BEFORE THE PUBLIC SERVICE COMMISSION

OF THE

COMMONWEALTH OF KENTUCKY

PUBLIC HEARING HAD ON THE 2ND DAY OF OCTOBER, 2000, IN LEXINGTON, KENTUCKY

ADMINISTRATIVE CASE NO. 384

BEFORE THE PUBLIC SERVICE COMMISSION, MARTIN J. HUELSMANN, CHAIRMAN, GARRY GILLIS, COMMISSIONER, AND EDWARD HOMES, VICE-CHAIRMAN.

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MR. HUELSMANN: Let's call this meeting to order. This is Administrative Hearing Case Number 384. For the record, my name is Marty Huelsmann, I'm chairman of the commission, and I'd like Mr. Gillis to introduce himself.

MR. GILLIS: I'm Gary Gillis, Commissioner at the Public Service Commission.

MR. HUELSMANN: And Ed Holmes.

MR. HOLMES: As Marty just told you, I'm Ed Holmes.

MR. HUELSMANN: And this is a formal hearing before us, and one of which we started. And the procedure for this was we passed out, but I want to go over a couple of preliminary things so everybody has an idea of where we're going.

This -- the PSC is very concerned about the rise of price of natural gas in the United States and in particular in Kentucky. We opened this case to investigate this increase as well as to investigate the availability of supplies, the procurement of gas by our five major local natural gas distribution companies.

And this is the first of our hearings. This is October the 2nd. We are in Lexington, Kentucky, and the featured utility is Columbia Gas. We intend to look at the course of recent price increases, the availability of supply for this winter and the future, and to look at how the gas companies are providing information to help customers, low-income customer assisted programs and disconnect policies.

In short, this is a fact-finding case in which we want to hear from all interested parties. The PSC wants to thank Secretary Viola Miller of the Cabinet For Families and Children, Secretary James Bickford for the Natural Resources Environmental, and Ron McCloud the secretary of the Cabinet For Public Protection, of which we're under.

These three cabinets are deeply concerned about the increase in prices, and we want to thank them in advance although some of them will be testifying here.

What we're doing today is kind of an experiment for the PSC. This hearing is going to be transcribed by that man over there, and his name is Allen McClung. He is going to take the transcript and have the transcript posted on our PSC web site next Monday. So those of you that would like to have a copy of what was done here, that can be reached at our PSC web site. That web site is www.PSC.state.ky.us.

The gentleman to the left is Adam Rabinowitz, and he is going to be digitally streaming this hearing;

which means that hearing will be taken in good quality. And once again, as use of an experiment that is going to be placed on our web site and it will be placed on the web site next Monday. So if you want to watch the hearing you can watch it then next Monday.

The order of business was placed and all of you have one of these; the order of the hearing. We're going to adhere to the hearing. We're going to -- with a couple of little changes. We need to make sure that we tell everybody who we are. And I'm going to have people introduce themselves very shortly. But the public, later on, when we have the public comments if you all would come up and sit right where Mr. Byars is sitting in the middle of that table, we will have the public testify from that standpoint. Otherwise it's going to be a typical hearing that we would have in Frankfort at our offices.

So with that in mind, would the staff introduce themself?

MS. MITCHELL: Anita Mitchell for commission staff.

MR. SHAW: Jeff Shaw with commission staff.

MR. HUELSMANN: And the lawyers for the Columbia Gas as well as the Attorney General's Office.

MR. TAYLOR: Mr. Chairman, members of the commission, it's Richard Taylor, Steve Seiple for Columbia Gas in Kentucky.

MS. CHEUVRONT: Emily Cheuvront and Dennis Howard for Office of the Attorney General.

MR. HUELSMANN: We have reserved time for a brief opening -- or brief statements by any local public officials. We have notified all the local officials of this hearing and we would like their input if anybody is here from that standpoint. Are there local officials here? I see none. We will then continue on with the hearing. And the first part of that hearing will be the testimony of the three witnesses that we have over there. I thought there was supposed to be four.

MR. SEIPLE: Just three, Mr. Chairman.

MR. HUELSMANN: Just three. Mr. Byars, would you state for the record your name?

MR. BYARS: Steve Byars. I'm the director of external affairs for Columbia Gas of Kentucky.

MR. HUELSMANN: And?

MR. PARR: Rick Parr, director of customer services for Columbia Gas of Kentucky.

MR. HUELSMANN: And how do you spell that, Rick?

MR. PARR: Parr is P-A-R-R.

MR. PHELPS: And I'm Scott Phelps director of gas procurement for Columbia Gas of Kentucky.

MR. HUELSMANN: What I thought we would do is swear in all the witnesses at the same time and you could put on your case and then they can ask questions. And when you all respond to the intervener or to our staff questions, tell who you are each question and that way Mr. McClung can take down who appropriately is saying that. So if you would stand up and be sworn, please.

(WITNESSES SWORN IN)

MR. HUELSMANN: Mr. Seiple or Mr. Taylor?

MR. SEIPLE: Thank you, Mr. Chairman. In light of our understanding of this proceeding we have some very brief opening remarks. If it would please the Commission we would like Mr. Byars to make some initial remarks followed by some brief remarks from Mr. Phelps.

MR. HUELSMANN: Thank you. Go ahead.

MR. BYARS: Mr. Chairman, Vice Chairman Holmes and Commissioner Gillis, we greatly appreciate the opportunity to be here this evening to discuss the situation that will affect every natural gas customer in the country this coming winter heating season, and that's the increase in wholesale natural gas prices.

As most of the people in this room probably already understand to a degree, the increase demand for natural gas the past few months has put pressure on natural gas supplies as well as the price of the utility, such as Columbia Gas of Kentucky, pay for natural gas and pass on to their customers dollar for dollar.

First, we would like to make it clear that Columbia does not view the situation as a supply problem. Gas supplies will be adequate to meet the public's heating needs for the coming winter. Columbia Gas of Kentucky will have plenty of the deregulated commodity. Unfortunately, consumers are going to pay more for the gas cost portion of their heating bills this winter.

Second, we would like to take this opportunity to thank the Commission for initiating this proceeding. There's no question that if this coming winter is colder than normal then we will see other state commissions initiate similar proceedings during the hearing season. We believe, however, the pro-active stance Kentucky has taken in this matter is appropriate. Collectively discussing these issues while it's 80 degrees outside is a thoughtful manner to determine how to react to a situation that will affect customers this winter, particularly low income customers, is clearly the appropriate forum.

In fact, this evening's public meeting is the perfect opportunity to educate customers about the factors impacting natural gas prices and to educate them further about the steps they can take to prepare, if they choose to do so, to help mitigate the impact of price increases on their household budgets.

Once again, thank you for the opportunity to be here. I'd like now to introduce Scott Phelps, Columbia Gas of Kentucky's director of gas procurement to give a more in depth overview of the factors affecting the increase in wholesale natural gas prices.

MR. PHELPS: Thank you, Steve, and I'm happy to be here tonight to talk about gas supply. I'm going to be focused on the business that we work on in terms of buying the gas from large producers and marketers, and how we are moving that gas to the market and what we foresee.

First, with regard - this will be pretty brief, about five minutes, but understand there will be plenty of time for questions later. With regard to the supply reliability as Steve has mentioned, we're on course with our storage injections for this winter and with contracting for firm gas supplies. We do that each year through and RFP or a Request For Proposal bidding process that’s negotiated afterwards to get the lowest price. Those negotiations are all completed and our contracts are in place. So it looks like, except for the commodity price itself, it looks like other winters to us.

We do not expect unusual problems with regard to providing reliable service this winter as compared to previous winters. We do not consider the current situation a crisis particularly in terms of supply availability. We’ve not had problems finding the gas that we’ve been injecting into storage. It’s a price issue. We haven’t been at a loss for finding supply.

The same is true for the RFP process. We did not encounter any difficulty to speak of in terms of finding the supply itself.

The price, however, as Steve has mentioned, is higher than we’re accustomed to. Most of us are probably here tonight because the price of natural gas in the open market has increased dramatically this past summer. And the current feeling is that those prices are bound to continue, at least for a while.

Analyzing how and why prices may have moved to this level makes me feel a little bit like the reporter that explains to us on the news the day after the stock market went up 200 points. If the reasons were as obvious as they make them sound on that day after we would all have bought the stock before that day happened. It's not that easy, because like gas prices the drivers and the timing are rarely obvious beforehand.

I think the prices have risen due to several factors that you can relate to the principles of supply and demand. I may need to cover just a little bit of history here as I get started.

Following the energy shortages in the 1970's, gas prices were deregulated at the wellhead. This deregulation resulted in more drilling to such an extent that we talked about a gas bubble for many years thereafter when describing the resulting over supply situation. This bubble kept prices at low levels for several years, but it also eroded the incentives for exploration and drilling by producers.

On the demand side, those low prices combined with environmental advantages, made natural gas very competitive with other fuels such as coal and oil; and that is particularly true in the large sector, in industrial markets and in the power generation markets. In addition, the continuing strong economy that we've experienced further supported demand from all customer sectors. With regard to weather, we've recently had a string of warm winters, which may have in part, masked the effect of a dissipating gas bubble.

In the near term predictions for a cold winter have been common. That is, this coming winter we've all read of different – or I've read various reports of cold weather conditions which helps to drive the mentality, at least, that prices will be high.

Finally, reports of storage injection levels that storage injections are below last year has probably created some more support for higher prices. But we really look at the storage levels as a result of higher prices and not as the root cause of them.

There are no doubt additional factors and explanations that some would list. But I think this is a pretty representative list for why the prices are higher today. As you might expect, higher prices have not gone unnoticed by producers. The number of drilling rigs has increased right along with the higher prices. This is what is supposed to happen when prices go up. People in businesses step in to fill a growing need. Even so, we cannot expect any production from these new rigs or new well drilling activities to really be bringing gas to market for the next – until the next 6 to 18 months.

Of course, like other commodities, gas will be – gas will continue to be affected by other factors as well, which will influence the price one way or another over the coming months and years. That is, that the expansion of the drilling program is not necessarily the only answer to this. Of course, there will be other factors as well.

That's the conclusion of my brief comments and I thank you.

MR. HUELSMANN: Is that all, Mr. Seiple?

MR. SEIPLE: Yes. That's the conclusion of our initial presentation. As I understand it, you would like our witnesses to be available for questioning by all the parties here tonight?

MR. HUELSMANN: That's correct.

MR. SEIPLE: And they are now available.

MR. HUELSMANN: Ms. Cheuvront, if you don't mind we'll deviate a little bit and let staff ask questions first.

MS. CHEUVRONT: That's fine.

MR. HUELSMANN: Would that be acceptable?

MS. CHEUVRONT: I thought that was the way it was going to go tonight.

MR. HUELSMANN: Ms. Mitchell?

MS. MITCHELL: Have any of the marketers or suppliers with whom Columbia currently contracts for natural gas supplies ever failed to deliver to the system?

MR. PHELPS: That's a question for me, I take it.

MR. HUELSMANN: Just a second.

MR. PHELPS: Oh, I'm sorry.

MR. HUELSMANN: Ms. Mitchell, would you ask that question again and speak up so that the audience can hear you. And you're going to have to –

MR. PHELPS: Say my name.

MR. HUELSMANN: -- Mr. Phelps, say your name when responding.

MR. PHELPS: Okay.

MS. MITCHELL: I'm sorry. I was asking if any of the marketers or suppliers that Columbia currently contracts for natural gas supplies has failed to deliver to your system.

MR. PHELPS: Yes, and no they have not. They're – you know, years ago we had some failures, but those people are not suppliers anymore. It's quite an efficient market now in terms of – in that case and we have not had any supply failures.

MS. MITCHELL: And I take it you have no reason to believe the ones that you're currently contracting with will fail to deliver?

MR. PHELPS: That's correct.

MS. MITCHELL: Is Columbia aware of any potential bottlenecks in the delivery system from the well-head to the city gate that could prevent delivery during this heating system?

MR. PHELPS: I'm not – in the normal term of a bottleneck I don't know of any bottlenecks. I mean, we have a good location here really on the western end of the Columbia transmission section and transmission system, and we are more or less blessed with the fact that the gas comes from the southwest so we're near the beginning of where gas has taken off. Most of the bottlenecks in this system are east of us several hundred miles.

MS. MITCHELL: Thank you. I wanted to ask if Columbia has reviewed its curtailment procedures for the coming heating system and if it believes these procedures are adequate?

MR. PARR: This is Rick Parr. Yes, we've already formed our yearly curtailment procedure review. And since we do not anticipate any supply shortage this heating season we don't foresee any need to make any changes in that curtailment process.

MS. MITCHELL: For the benefit of the members of the public, will you identify the different components of Columbia's wholesale gas cost and explain the extent to which these components are or are not subject to regulation?

MR. PHELPS: The components of the wholesale prices?

MS. MITCHELL: Um-huh.

MR. PHELPS: Let me break that down into three components for you. The first and largest one is typically the gas commodity price itself, buying volumes of gas. That price as I mentioned a little while ago was - is deregulated. It used to be - years and years ago it used to be regulated by Washington, the federal agencies. But today that's not regulated. It operates in an open free market. It has a future's contract associated with in on the New York Mercantile Exchange. So it's, I would say, totally deregulated, in that respect.

The second portion of our wholesale commodity cost is related to paying the pipelines for the transmission capacity required to get the gas from where we buy it up to our Kentucky city gates. And that is really broken down into two components of its own. We pay a demand charge on the contract volume itself. And we pay a commodity charge, which is a smaller charge that's billed on a per-unit used basis. Both of those charges are regulated by the Federal Energy Regulatory Commission and are approved rate schedules and tariffs of the pipelines.

And I would – you know, I would add that in that sense that component is regulated. All of these costs go through our GCA mechanism if you're here in the state, here in Kentucky. And, of course, that gets approved and reviewed by the PSC, I think, on a quarterly basis.

MS. MITCHELL: Okay, thank you. In reference to item two of the Columbia's response to the commission's recent data request, the last sentence under part A you refer to, colder than normal design winter conditions. Would you describe or define what colder than normal winter – design winter conditions is?

MR. PHELPS: Sure. In our planning process we use the term "normal" to designate many years of – the average of many years of statistical data about temperatures in Kentucky. And those temperatures range at different locations. Some of them go back 40 years, some of them go back as far as 60-70 years. But we utilize all the data that's available to us historically to determine a normal, an average.

And the colder than normal scenario is what we prepare for on a contract portfolio basis. That's what we would go out and make sure that we could cover on a firm basis to serve a firm retail market. So we have the volume, the demand the firm retail market will consume on both a daily and a winter season basis. The coldest day and also based on a winter season cold.

In both of those cases the design is based on a temperature that has a probability of occurring one in ten winters. It's called one in ten probability of occurrence. In terms of how cold that really is, it's not exact – it's not exactly a ten percent colder than normal winter. It's a little bit different. And I think in Kentucky it's a little bit higher than ten percent. But what I mean is there's ten percent more degree days in that winter than in a normal winter.

The same sort of analysis is done for peak day planning. So we need firm capacity to hit the peak day, and we need enough firm capacity delivering supplies to cover a cold winter. It's two different design parameters.

MS. MITCHELL: And what is the temperature that is used to based those design - I mean, you stated that you go back -

MR. PHELPS: That design temperature, which is the average over the whole 24-hour period. It's not what you think of when you think about how cold did it get today, but the average for the whole day is minus four degrees.

MS. MITCHELL: Minus four?

MR. PHELPS: Um-huh.

MR. HOLMES: Could you ask that question again? I think some of the audience couldn't hear.

MS. MITCHELL: I'm sorry. I asked him - the first question I asked him, if they could describe to us what a colder than normal design winter condition was. And then he was explaining how they did that. So I asked him what the temperature was that they based that on.

MR. PHELPS: The temperature was minus four.

MS. MITCHELL: And referring again to the data responses that you submitted on behalf - that was submitted on behalf of Columbia, in item four the response to the commission's data request compares customer's average bills in January 2000 with what those bills would have been based on the rates in effect as of September 1, 2000. Based on an average residential usage of 17 MCS in January, this comparison shows that a residential customer's bill would increase from $128 to $159. Is it correct that the only changes in rates from January 2000 to September 2000 result from increases in Columbia's wholesale gas costs?

MR. BYARS: Yes, that is correct. There has not been an increase in base rates during that time period or as it appears on customer's bills, the delivery charge. That increase during that time period is due to the increase in the wholesale natural gas costs and the related adjustments that go through the quarterly gas cost adjustment.

MS. MITCHELL: Thank you. With regard to the natural gas that Columbia currently has under contract, how do you determine that the contract is prudent and reasonable? In other words, what bench marks or industry averages are relied upon by Columbia?

MR. PHELPS: Well, first of all, I indicated earlier that we do run a fairly extensive request for proposal. That's a bid process where we send requests to all of our suppliers, and there's generally about 40 of those in terms of major suppliers that we work with. You know, they're pretty much forced into a competitive marketplace.

It's not – it's quite a transparent marketplace. There's not a great deal of hidden costs in the way gas is bought and sold today. You can compare – on a daily basis we're looking at Internet services that provide places to buy and sell with bid asked prices. And we don't use those yet in terms of actual purchasing, but the industry uses them to a great extent in terms of pricing and comparing. We determine where we think prices are going and – on any given day – and move that price down as far as we can.

We're talking about pennies here on four dollars worth of gas or five dollars worth of gas. We're talking about trying to move that a penny or two one way or another in negotiations. The same is true on the RFP process.

In addition, there are monthly indices that are based on surveys of prices paid and prices bought, which a good number of buyers and sellers use as parts of the contract pricing mechanisms.

There's a lot of transparency in the market place is the point I'm trying to make. And what we do is try to push the price down to the lower end of that range.

MS. MITCHELL: Okay, thank you. In item five of the response to the commission’s data request in part F refers to the Columbia’s mix of spot purchase short-term and long-term contracts. Will you identify and describe the factors that affect the mix chosen by Columbia, a mix which appears to favor spot purchases and short-term over long-term contracts?

MR. PHELPS: Scott Phelps. I remembered. The – yes, I’d be glad to. We have – let me define those terms at least for the folks who may not be as familiar with it. We call short-term contracts contracts of 12 months or less, and long-term contracts contracts that exceed 12 months. Spot gas is bought for – generally speaking, spot gas is for 30 days or less. Often spot gas is bought for one day.

The basic distinction in our portfolio is that short-term and long-term contracts are about as firm as they get. And the spot contracts are more flexible and can be agreed to on an interruptible basis. There’s a good deal more flexibility from week to week and month-to-month dealing with spot gas.

In addition, firm gas, short-term or long-term, is – the market is such that you pay a small premium over the market index price for that gas. So whenever we are not in a – when we're not dealing with a reliability issue – for example, June, when we're filling storage and there's not likely to be an interruption or a problem on a system, we depend heavily on spot gas in hopes that that will add some price savings to the mix.

Spot gas is also a more flexible tool. Months like October, the week we are in – an 80-degree day is one of our most difficult days, really, because we're trying to max out storage. At the same time storage is very difficult to put much gas in. And a warm day in the shoulder month, we call them like October and November, are difficult days. So the spot gas gives us that kind of flexibility. We can buy gas one day and not another day. And the goal on those days is to avoid pipeline penalties.

The difference between long-term and short-term, that issue is, you know, we perceive through our market bids and so forth premium paid for long-term. You know, basically there has not been a supply problem with any of these contracts or any failures. So we are – we move to the short-term agreements more than the long-term to add flexibility to the portfolio, to deal with weather situations and to save a few pennies. Well, a few pennies multiplied by a lot of volume.

MS. MITCHELL: Thank you. Will you tell us how Columbia determines the volume of gas it will purchase from each of its suppliers?

MR. PHELPS: Well, there's different arenas. There's the long-term or short-term RFP process, that firm contract mix that we look for, and there's the spot gas. In spot, you know, absolute price is a heavy driver and we look for the suppliers that we know will deliver, and the best price of the mix, and the volume that they've got available.

On the term gas, we're trying to develop not only the absolute minimum price, but we're also trying to develop a portfolio that will have less risk associated with it for failure. So we will end up with several suppliers for firm gas on the short-term contracts; and that ends up being the case on the spot too. I mean they go back and forth in terms of which one's cheaper this day.

But, you know, we try to maintain strong relationships with several suppliers, because when you have difficult times in terms of reliability or places to put gas on a hot day or, you know, all the issues that come in on a day-to-day operational business you can't depend on one trading partner or supplier. You need several. And as I mentioned earlier we weigh that risk of dealing with one or two people versus mitigating the risk. And we'll spend an extra quarter of a penny or something to get that, you know, that diversification.

MS. MITCHELL: You may have answered this question by what you just said, but does Columbia take the maximum volumes possible from the lowest cost suppliers?

MR. PHELPS: Yeah, I kind of answered that question. I guess yes and no. I think the, based on what I said – there's a limit to how much you'll take from one supplier. And as I mentioned, it's a very transparent market. Nobody is killing the other guy on price.

MS. MITCHELL: In referring to item five of the response to the Commission's Data Request, Columbia identifies natural – Columbia Natural Resources or CNR as the only affiliate from which Columbia is currently purchasing gas or has purchased gas during the past 12 months. In your opinion, is the price that Columbia pays CNR subject to the affiliate transaction pricing rules contained is House Bill 897 that amended KRS 278010 through KRS 278450?

MR. PHELPS: It's our understanding that during – it was our understanding during the crafting of that legislation that the bill applies to retail products and services only.

MS. MITCHELL: Thank you. Will you tell us what type of pricing is reflected in Columbia's purchases from CNR, are they spot purchases, short-term or long-term?

MR. PHELPS: This is Scott Phelps. Pricing and the term length of the contract are not necessarily synonymous.

MS. MITCHELL: Okay.

MR. PHELPS: But we have talked about the length of and the term of the contracts. And the CNR contract qualifies as a long-term contract in terms of its length. The way we price long-term versus short term is both are tied to market indices that are similar in nature. So just the fact that it's long-term or short-term doesn't change the price characteristic.

MS. MITCHELL: Okay.

MR. PHELPS: But it's a long-term contract.

MR. HOLMES: I just have one question. This is Commissioner Holmes. When you purchase from CNR is that then through the RFP process as well?

MR. PHELPS: The CNR contract is a contract that purchases local Kentucky gas to serve customers that we have that are directly off of those local gas gathering lines, and that’s why we contracting with CNR because they own those gathering lines. There isn’t another – there isn’t anybody else to send the RFP to.

MR. HOLMES: Okay, thank you.

MS. MITCHELL: Does CNR sell gas to local distribution companies other than Columbia, to your knowledge?

MR. PHELPS: Yes, I think they do.

MS. MITCHELL: Does CNR price the gas it sells to Columbia differently than the gas it sells to other gas utilities?

MR. PHELPS: I have no idea about how to answer that. I haven’t seen their contracts.

MS. MITCHELL: Okay.

MR. PHELPS: I would assume that that’s similar.

MS. MITCHELL: And how does Columbia determine the volume of gas it will purchase from CNR?

MR. PHELPS: These markets that are being served, these homes that are burning the gas are, as I said, are coming directly off these lines. So what we do is, the volume is determined by how much those customers burn. We read those meters and determine the volume purchased at the end of each month. So that contract is required to swing up and down, do all the things that we would normally try to do with storage and things – and other assets, and that's all taken care of by the CNR agreement. Again, it's the volume used by the customers off their line.

MS. MITCHELL: In item five, again, referring to columns three and four of the table that was included in that response, it appears that during 1999 and 2000 Columbia purchased from CNR – I'm sorry, just a minute. I'm sorry.

Will you provide an overview of Columbia's disconnection policies and the type of modified payment, partial payment plans available to customers that have difficulty paying their gas utility bills?

MR. PARR: Yes. This is Rick Parr. I'd like to take you very briefly through our collection process from start to finish. Collection process begins at the time the bill is generated and mailed to our customer and provides approximately ten days as a due date for that bill. If the balance is not paid approximately five days after that due date a termination notice would be issued to that customer providing them another ten days before termination could possibly actually take place. So in all, there's approximately 29 days from the date the bill is generated and mailed to the customer before they could possibly be subject to termination for non-payment of that bill.

At any time during that period we encourage any customer that's having payment difficulties to contact our office. We can generally, normally work out a mutually agreeable payment arrangements for those customers.

As far as the different types of payment arrangements, we generally try to customize that payment arrangement to whatever the customer can pay us. One payment arrangement we do offer is our budget payment plan, which spreads the cost of gas evenly throughout the entire year. We have about 50,000 of our customers who now take advantage of that payment plan and appear to enjoy it or like it very well.

MS. MITCHELL: Thank you. Has Columbia considered any tentative plans or contingency plans to liberalize those disconnect policies or payment plans if the increase in price –

MR. PARR: This is Rick Parr. I'm sorry.

MS. MITCHELL: -- if the increase in gas

prices significantly increase?

MR. PARR: We haven't made any specific plans at this time to liberalize those policies. As I mentioned, we have always made every effort we possibly could to work with our payment trouble customers to prevent termination of service. We plan on continuing to do that, do whatever we can do to make certain that arrangements are available for customers to spread payments over a longer period of time if necessary.

MS. MITCHELL: In response to item seven of the Commission's Data Request, there was identified various assistant programs for low-income customers, while the response to item nine discusses universal service fund as a possible means for providing assistance to low-income customers. A universal service fund is referred to as more comprehensive and less confusing and complicated for customers. Is this in comparison to the low-income assistance programs currently available?

MR. BYARS: Yes, it is. We're very fortunate with Columbia Gas of Kentucky that the lion's share of our customers are served by the Community Action Council here that serves Fayette County and some of the surrounding counties. And they operate several programs, actually a myriad of programs for low-income customers on energy assistance as well as other types of programs as well.

The Columbia's customer assistance program, in fact, has been a partnership with the Community Action Council for many years. I think they would probably agree that today customers have to kind of follow a maze to figure out which program works best for them or which program actually has money left to serve them during the winter heating season.

A customer may talk to Columbia Gas, a customer may talk to Community Action Council, may talk to a variety of people to try to find the program that fits best for them, or, again, if a program actually has money available for them. We think a universal service fund could be more comprehensive than that, serve a wider range, array of customers and hopefully make it less confusing for those customers to figure out which program was actually available and had money still left during the winter heating season.

MS. MITCHELL: Would you envision that a universal service fund would replace the programs that are currently available?

MR. BYARS: I think it depends on what the universal service fund looked like, how well it was funded, out comprehensive the design was. As I mentioned before, we have a customer assistance program with the Community Action Council. We've committed to that program through 2004 and we'll stick by that commitment no matter what happens with the universal service fund in between now and then.

We think that that program does a very good job at serving the neediest of the needy. So it may very well be that programs like that are still necessary to serve that type of low-income household. Or it may mean that if the universal service fund is well enough funded and designed to be comprehensive enough to serve a variety of low-income customers that those kinds of programs aren't necessary any more.

MS. MITCHELL: Okay. In response to item ten of the Commission's Date Request, Columbia identifies strategies that could mitigate the impacts of higher wholesale gas prices. Is it correct that the strategies identified in the response are strategies that are currently employed by Columbia as part of its gas procurement process?

MR. PHELPS: Scott Phelps. Yes, that's the intent of that answer. Those are all currently used.

MS. MITCHELL: Does this cover the full gamut of possible strategies or are there other gas procurement strategies that have been considered and rejected by Columbia?

MR. PHELPS: In terms of mitigating or reducing costs, yes, I believe it’s complete. We have considered hedging programs either using financial instruments or directly with the supplier using fixed prices. The end result can be the same thing. But we view those – we view that as a way to mitigate volatility as opposed to reduced price.

When you hedge you are likely – one of two things is going to happen. You’ll end up paying more than you otherwise would have or you’ll end up paying less than you otherwise would have. And so most folks when they’re talking about hedging they’re talking about hitting the middle road there, and that means you’re going to – you’re going to save half the time and lose half the time.

MS. MITCHELL: Columbia recently initiated a customer choice program that permits residential customers to choose their own gas suppliers rather than purchase from Columbia’s system. Do you believe the choice program offers a residential customer the potential to mitigate or avoid the increase in their gas bills due to the increase in wholesale natural gas prices?

MR. BYARS: Steve Byars. Yes, we do. That is exactly why we initiated the customer choice program and took it before the Public Service Commission for their approval. We think it provides customers an opportunity to somewhat control their natural gas costs, some control that our large industrial customers have been exercising for more than 20 years now. And we hope and we've seen already, as a matter of fact, that marketers have been able to offer some rates to save some customers money on their gas bills, on the gas cost portion of their bill.

It should be noted though that marketers purchase their natural gas from the same wholesale market that we do. And that as a result it's probably impossible for a customer who participates in the customer choice program to completely avoid the increase in natural gas prices that we've seen on the wholesale market. But we have seen an opportunity already at a very early stage in the program, seen opportunities for customers to save money on their gas bill by purchasing their gas through a marketer.

MS. MITCHELL: In response to item 11 of the Commission's Data Request, Columbia stated that the market is working the way it should, is suppose to, and has responded to the basic law of supply and demand. It also cautions against short-term regulatory fixes that may rob the market's ability to work as it should in the future. From this response, is Columbia advocating a hands-off approach to increases in natural gas prices?

MR. BYARS: No, I wouldn't put it that way. I think that, as I indicated in my opening remarks, that this case is a very appropriate proceeding to discuss how the rise in wholesale prices will effect all natural gas customers, particularly low-income customers, and to see how we can best react to that situation that we know is inevitable.

We believe that there are certain things that can be done and can be done right away and, as a matter of fact, have already been done, and are undergoing, that can help that process. We can continue to educate customers about the factors causing the volatility in the natural gas market place. And this hearing is the first place to do that. We can continue to educate customers on how they can reduce their energy consumption.

When we go out and make presentations about customer choice we take brochures on winterization and conservation with us. We continue to educate customers about the options available to them under the customer choice program. And through our speaker's bureau, making presentations to neighborhood groups and other civic groups, two or three a week, and the requests keep rolling in.

Continuing to education customers about Columbia's budget payment plan program that can help spread those costs evenly out over and entire 12-month period. As we already indicated, stand ready if necessary to help customers who may need short-term assistance in dealing with high energy costs.

MS. MITCHELL: We had one question sent up from the public and we only have one, do you want me to -

MR. HUELSAMNN: There's one question from the public? Why don't you go ahead and ask that at this point, Ms. Mitchell.

MS. MITCHELL: There's a member of the public that has submitted a question. They have a concern. They wanted to know has Columbia Gas of Kentucky cut back on their service to customers. They relayed that having been advised that they no longer restore service after a customer cut off for leakage. No safety inspection on this or transfer of billing, transfer of billing may be done by computer. No service person sent to the premises. I guess their basic question is, has Columbia Gas of Kentucky cut back on service to its customers?

MR. PARR: Rick Parr. No, we have not cut back on our service to our customers. What we have done, and specifically the question I believe addresses the situation where leakage could be found at the property. In the past, we have required that a Columbia service person return to the property after a qualified plumber had already made repairs, which meant the customer had to wait until we could schedule a service person to be there to restore their service.

The qualified plumber who's making those repairs can restore that service without a second visit from Columbia. So what we've done is simply allow the customer to have a leak repaired more quickly and have their service restored immediately upon repair by the plumber.

MS. MITCHELL: Okay, thank you.

MR. HUELSMANN: That's all you had?

MS. MITCHELL: I have no more questions.

MR. HUELSMANN: Ms. Cheuvront, do you have any questions?

MS. Cheuvront: Yes, I have a few. Thank you. Emily Cheuvront with the Attorney General's

Office. Good evening.

MR. HUELSMANN: You might want to spell that for the court reporter.

MS. CHEUVRONT: Oh, I'm sorry, okay, C-H-E-U-V-R-O-N-T.

Mr. Phelps, you said there was other factors than just supply that was causing the increase, or that's what I understood you to say. Could you give us an idea what the other factors are?

MR. PHELPS: I guess I'm thinking back to near the end of my first presentation where I said that there's new production going to come on-line or, you know, the producers have got – have increased their rig count 40 percent or something in the recent months. And my point was, yes, there's more supply. I just didn't want you to take away that that's the answer and that's the only thing that counts. It's one – it's just one of those many things.

The other things that I mentioned leading up to it still apply. What happens with demand, is gas still competitive with oil at the power plants. You know, just a lot of other things. What's happening -- you know, sometimes what's happening in the Middle East. Things that just – just because you solve maybe one part of the puzzle doesn't mean other things in the market don't keep changing.

MS. CHEUVRONT: Thank you. You also stated that even though we're seeing new supply, it's going to be a while before we see any change in the prices. What's a while?

MR. PHELPS: Let me say I don't know when prices will come down or go up. For example, people -- the market knows that we're going into the winter. The market knows that customers need to go into the winter with supplies in hand and gas in storage. I'd be very surprised if we had large drop offs in prices just before the winter, for example. But with the other factors I'm talking about if we get in to November and we get into December and we've had a warm winter, I think there's going to be gas on the market, as an example, and prices could drop.

The futures market today, the futures contracts are an indicator, but that doesn't mean – and they might say that prices are going to be $5.20 in January. Well, we'll find out what January is on December 28th, basically. And there's – if it's really cold it will mean one thing. If it's really warm it will mean something else to price.

I'm not a big predictor; never have tried to be. And I don't want to start right now.

MS. CHEUVRONT: Do you see it that at least maybe leveling off? If not going up and down maybe hitting a level? I know I just asked you to predict.

MR. PHELPS: No, I don't see it leveling off. I see it continuing to go up and down.

MS. CHEUVRONT: Up or down.

MR. PHELPS: Yeah.

MS. CHEUVRONT: Do you know what you paid for gas last year at this time compared to what you're paying now, and then what you paid - are paying now at this time?

MR. PHELPS: Somebody might be able to help me, but there were - in 1999 there were prices in the mid two dollars to - and rising up over time through like $2.80 per decatherm. A decatherm is a million BTU's. Today that same price is more like five dollars.

MS. CHEUVRONT: One of the things that you said that you're doing is trying to help your customers get on or educating your customers about the budget. My understanding, and correct me if I'm wrong, is August is when you have sign up for your budget?

MR. PARR: Rick Parr. No, actually you can join the budget payment plan anytime during the year.

The benefit of joining in August is that you begin to build a credit on your bill so that when those higher bills in the winter start to hit you reduce that credit and pay for some of that usage in the winter from a credit you've already built in August. If you join later in the year, your budge amount would be established at a higher level to begin with.

MS. CHEUVRONT: Can anybody join the budget? What's your qualifications to be on the budget?

MR. PARR: Any residential or commercial customer can join the budget payment plan.

MS. CHEUVRONT: Do you reassess, recalculate every quarter and maybe adjust the budget?

MR. PARR: Yes. We calculate the upcoming season's budget in August of each year. In March we do a review and determine if we feel that based on weather conditions and what you're budget was originally established at, if we feel that that amount is going to be too high or too low.

The ultimate goal is to pay you out to zero in July of each year and not either us request for you to pay a large amount to settle up or us keep a lot of your money and have to refund that to you in July, one or the other. So we try to make that adjustment in March of each year to make certain you're paying the right amount each month.

MS. CHEUVRONT: And one of your recommendations that you said that you stand ready if necessary to help customers. Were you referring to your liberal approach towards working out some kind of payment plan? Does that what your, stand ready –

MR. PARR: Yes, correct.

MS. CHEUVRONT: Could you explain, because I know this is what – questions I get from consumers is you say your gas is a pass through. So first thing in your mind is then, okay, how can I save money by customer choice? So we can understand.

MR. PARR: I know it sounds – it almost sounds counterintuitive or illogical to say that, and believe me, that’s a good question. We get that every time we go out and make a presentation on customer choice is how can a marketer do better than you can if you guys are simply passing that gas cost on through and not making any money on it. The best way I think to answer that question is that marketers, as they are unregulated, have some ability to in their ways to purchase natural gas and in their ways they can be a little bit more flexible in their pricing of natural gas to our customers than we as a regulated utility do.

Today the way things work is if a marketer may use some techniques to purchase natural gas that we as a regulated utility cannot employ, then that risk is passed on to the marketer not to the customer. And the flip side of that is that they're willing to take the upside as well.

Today if a utility company tried to take advantage of some of those same techniques then the risk would be passed on to the customer as opposed to a marketer or somebody who's willing to take both the risk and the reward.

MS. CHEUVRONT: You said you determined that you were going to have enough supply by your firm retail customers. Not knowing, since we just started customer choice, what customers you're going to have, how did you decide what you firm was? I mean, what if nobody leaves?

MR. PHELPS: That was a good question. Scott Phelps. My planning guy is not here right now, but I'll try. The – we do try to forecast that. And there has been some experience gained in other areas that we serve, at least in the Columbia group. And so we're using some of that experience to make the forecast.

The initial numbers, at least for this

coming year, are not huge. And so there's some flexibility granted to us this year. But each year we're going to be trying to forecast that. And it's based on experience and trends, and that's the answer. I mean, we'll forecast it and buy the remainder.

MS. CHEUVRONT: Do you know how your contract with your affiliate CNR compares to the other contracts price wise? You say there's not much really flexibility, they're pretty close?

MR. PHELPS: It's a much different contract. It's local gas in a unique area that swings every day. What I mean is it goes up - the volumes go up and down unlike anything else I've got. So it's difficult to compare it. But they're all driven by market indices. Whether it's a large supplier in Houston or CNR in Kentucky. We look at the local market indices and negotiate from there. They give us services and guarantees and we negotiate a price.

MS. CHEUVRONT: You recently got approved by this commission for a merger or acquisition by NiSource. Is it completed?

MR. PHELPS: No, it's not. It doesn't have SCC approval yet.

MS. CHEUVRONT: Are you still dealing as separate and distinct companies then?

MR. PHELPS: Yes.

MS. CHEUVRONT: Do you know when to expect that to be completed?

MR. PHELPS: I'm not an expert, but I've read that it should be very soon - or it might be very soon. Let me put it that way.

MR. SEIPLE: Let me just add this to the record. NiSource has said all along that they expect all the regulatory approvals by the end of this calendar year. And I believe that is still their estimate. They expect approval before the end of this calendar year.

MR. HUELSMANN: Thank you, Mr. Seiple.

MS. CHEUVRONT: In the hearing, I believe it was said that the merger is going to produce some savings? Do you see these savings, though it's not in the gas cost, is there - will the savings maybe - will there be savings in the base rate that we will see that can maybe counter some of the higher gas costs? Am I being clear?

MR. PHELPS: Are you referring to statements made in the case regarding savings in the gas costs or other related savings?

MR. HOWARD: If I may offer some explanation. Dennis Howard, Attorney General's

Office. In the actual hearing itself, statements were made, as I recall, from the company that due to the merger of the two companies leverage would be had in order to purchase gas at lower costs. Plus, there would be lower costs for the gas because of the use of the distribution line of transmission. So the question that we would have at this point in time, are any of those savings available to the customers?

That’s a compound question. First of all, do you recall those statements being made? And then second of all, if so, are those savings being realized at this time?

MR. BYARS: If my memory serves, I think that was in the prepared testimony of the case. The merger hasn’t actually closed yet. As Mr. Phelps indicated we hope to close that before the end of the year, but we haven’t integrated the two companies yet so there have not been any benefits related to the merger or related to gas costs.

MR. HUELSMANN: You do still expect some savings to take place?

MR. BYARS: Testimony has not changed. Yes, Mr. Chairman.

MS. CHEUVRONT: Do you know when? Will we see it in this gas crisis?

MR. BYARS: I doubt it.

MS. CHEUVRONT: I know, predictions.

MR. BYARS: I guess – the reason I smiled to myself at first I guess we don’t – I guess it depends on your definition of crisis. It’s – as Mr. Phelps indicated we don’t know exactly what prices are going to do, but I guess we want to make it clear that, from a supply standpoint, we don’t look at this as a crisis.

From a prediction standpoint on when the merger will close and how the companies are integrated, I guess I would be a little bit surprised – I’m conjecturing a little bit – but I would be a little bit surprised if we saw that this coming heating season just because it will take some time for the two companies to actually integrate and put the two companies together.

MS. CHEUVRONT: I believe I just have one last question. Does NiSource own any of the entities in your gas supply chain?

MR. PHELPS: Looking at the two companies as we have been in the past, no. No, they don’t.

MS. CHEUVRONT: That’s all I have.

MR. HUELSMANN: Is that all you have?

MS. CHEUVRONT: Thank you.

MR. HUELSMANN: Commissioner Gillis?

MR. GILLIS: I just have a couple of questions. You indicated that the – I believe Scott did, Mr. Phelps, that the commodity cost has gone up from about $2.90-$3.00 a year ago to about five dollars now, which is about a 65 percent increase in the gas cost itself. Although the overall cost I think is what, in the neighborhood of 30 to 50 percent for an average bill this year versus last year; is that correct?

MR. PHELPS: If I may, the increase from – I apologize, I don't know the difference between this time last year and this time right now. Our last quarterly adjustment that we submitted to the commission a customer's bill went up – an average customer, residential customer's bill went up 20 percent because of the wholesale increase in natural gas prices.

MR. HUELSMANN: Do you want to just consider that a data request at some time.

MR. GILLIS: Well, if the numbers I have, and maybe you have them there close, is that the expected gas cost presently is 6.26 versus 4.44 last year, this year versus last year, most recent. But I'm really getting to the fact that it's going up some percentage. I'm not sure what it is. And what do you anticipate, what is your assessment of the increased defaults as a result of that come winter and sort of discuss that just a little bit.

MR. PHELPS: I didn't hear the last couple --

MR. GILLIS: I guess that's probably a Rick question.

MR. PARR: Rick Parr. Could you repeat the question, please?

MR. GILLIS: I was saying because of the increase in cost, the average bills are going up considerably, 30 to 50 percent or whatever the percent might be. And therefore it's going to be – there are going to be a lot of people that are going to have a hard time paying their bills, which in turn would cause increased defaults or probably disconnects. Can you discus that and discuss contingency planning and maybe what you all have talked about and what you're going to do?

MR. PARR: Well, first of all, I think it's very hard for us to predict the percent of additional defaults over previous years. A lot of that is going to depend on the weather itself. If we have an extremely mild winter, yes, bills will increase, but not to the same degree if we have a very cold winter.

So I hate to make a prediction as to how many additional customers would fall into that payment trouble category. But as I mentioned earlier, we're planning on and have every effort to work with those customers and make whatever arrangements we need to make to allow them to keep service during the winter months.

MR. GILLIS: Now I guess what I'm saying is that this is unusual. We anticipate it being unusual. If it continues as we are going presently with the increased cost that there will be additional defaults. And I was, I guess, really looking for a worst case scenario on what might happen and whether you all will decrease personnel, if necessary, to work with those that might need assistance or what contingency planning might have been done, if any?

MR. PARR: We haven't really made any contingency planning at this point. We feel we have sufficient staff to respond to all those customer's inquiries. Our statistics in our customer service center bear out that we can quickly and efficiently answer those customer's inquiries. And I believe that we will be able to work with them all through the winter months.

MR. HUELSMANN: Mr. Holmes?

MR. HOLMES: I just have a couple also. I had a question on your process, the RFP process. What goes into that RFP to ensure that you are acquiring the lowest cost of gas available?

MR. PHELPS: Scott Phelps. Every spring, around the beginning of April, we identify 30 to 40 suppliers that we work with and we feel pass muster in terms of credit and reliability and their ability to provide good service. And we identify each stream of gas, in other words, which pipelines we need to move the gas in. We identify all of that and ask for some fairly specific bids in the mail from them. Time out.

And once we get – we ask for some very specific bids in the mail. Those people who we've identified as being strong on one pipeline or another, they're the ones that are getting that opportunity from us. And we'll sit down and review these offers. We'll determine – we'll compare their – the kind of service that they're offering in terms of the day-to-day swing. We'll compare the premium over index that they expect to be paid. And we'll try to set – we'll try to set the low market that we think – where we think it should be and we'll begin negotiations to pull people down to that market.

It's not a simple RFP process where we just receive it and the contract is signed. The RFP, that terminology we really use that to open up negotiations and to get some competitive bids just to know, to get a better feel for where to start negotiations. Try to bring everybody down to the lowest number.

MR. HOLMES: Thank you. Do you purchase for the entire Columbia system then or –

MR. PHELPS: All of the Columbia local distribution companies.

MR. HOLMES: In your schedule of purchasing, how do you determine which LDC gets gas at which time or which LDC gets the lowest available gas? I mean, Kentucky versus Ohio or Kentucky versus Pennsylvania?

MR. PHELPS: I'm tempted to – I'm tempted to say Kentucky always gets the lowest, but I'm not going to say that. In the RFP process we actually sign the agreements on a multiple basis. If we were to sign a contract with Texaco, for example, we'd sign five contracts. It's got the same price in it. And it's got – it gives us some flexibility.

If we sign the contract with Texaco for a volume per day, 50,000 decatherms or something like that per day, having the five local distribution companies allows us to make better use of that contract, if it's a good contract, all the time.

But what we'll do is we'll take Kentucky, for example, and Kentucky will get a designated portion of that 50,000. And it's all – let's – for example, let's say it's – there's an index called Inside FERC Onshore Louisiana first of the month and that's the way it's priced.

The contract will say that and it will say, plus one or two cents. That's the contract price. Ohio pays that. Kentucky pays that. Maryland pays that. Because those are all – because that contract is all – has the benefit of all being at the same receipt point on the other end of the pipeline. We have to buy the gas at certain points to match up with our transportation contract so there's some commonality there.

A little bit different process is in spot gas supply where we're buying gas through a two-hour period and we're trying to get a certain amount in for each company, hit that target. What we're going – if the gas happens to be at the same point of receipt, we're balancing it out so that, you know, the average of the day is coming within fractions of a penny.

MR. HUELSMANN: We need to take a little break so the videographer can put in a new tape.

MR. HOLMES: That was my last question.

(OFF THE RECORD)

MR. HUELSMANN: Have you seen any increases in wells in Kentucky being drilled for natural gas because of the price going up? Are you aware of any?

MR. PHELPS: I'm not personally aware of those details, but I think that the interest in drilling is widespread. And I would be surprised if there weren't new wells being drilled in Kentucky.

MR. HUELSMANN: Do we have enough natural gas based upon last year's temperature to – for heat in Kentucky for this next winter?

MR. PHELPS: Yes. All the gas to cover the cold winter and the peak day is contracted for. Storage is, today, we're running at about – we're still injecting and we're at about 95 percent of our total contract quantity.

By the end of the month, which is the last month of injection, October, going into the November winter season where gas starts to come out of storage we should be at 99 percent on the last day of the month. That's our goal. And we leave that one percent sitting there really in case November 1 is a warm day and we have to inject on the spur of the moment to avoid penalties, injection penalties. So, yeah, we're right on target.

MR. HUELSMANN: If we have a winter like 1977 or 1978 is there going to be enough gas for the citizens of the Commonwealth of Kentucky through Columbia?

MR. PHELPS: That's a couple years before I got here, but I – just a couple. I got here in '78. So I don't think there's a problem in that respect. I think that even if – and I don't remember the percent cold or the normal in 1977, but assuming it was more than 10 percent the way we would accommodate supplies over and above that is to be – we'd have to be also out aggressively in the spot market on the days where gas would flow and that's how people get through colder than designed periods.

MR. HUELSMANN: Thank you. Mr. Seiple, do you have any further –

MR. SEIPLE: No, I have nothing further.

MR. HUELSMANN: Ms. Mitchell?

MS. MITCHELL: I have nothing. Thank you.

MR. HOWARD: Yes, Mr. Huelsmann, a few more if I may, sir. Would you be kind enough to explain to me the procedure in place, and I think it's under law, for shutting off someone's gas?

MR. PARR: Our termination procedures are in compliance with our approved tariff. I don't believe there are any laws that say service cannot be terminated at any given time. As a matter of fact, I'm sure there's not. We make a concerted effort during the winter months when service or when, I should say, temperature falls below a certain point that we make a decision that we will not terminate service during that time period. That's a company position.

MR. HOWARD: And Mr. Parr, you explained earlier that you attempt to work with the customers in regards to payments plans if they are in default?

MR. PARR: That's correct, yes.

MR. HOWARD: And currently, perhaps this is for Mr. Phelps, given the fact that in your contracts there are certain projections that you need to make in order to determine a price that you want to pay for gas; is that acceptable to you? You have to involve yourself with certain projections in determining what you should or should not pay for the gas itself?

MR. PHELPS: Well, I have to – if I'm understanding you correctly you're talking about volumes, how much to buy?

MR. HOWARD: The volumes and perhaps even the price. Would that not apply?

MR. PHELPS: What we're forecasting or projecting is the volume, the amount of demand our customers will have. The contracts that we – now these folks in filing gas cost adjustments have to also have a forecast of price. But in our side in terms of knowing how much to contract for I need a volume estimate.

On top of that if the volume was too low – I mean, I shouldn't say too low, but if the volume was lower than expected, I have flexibility negotiated into the contracts. I don't have to take every decatherm that I contract for. And the way we've negotiated it, there's not necessarily a cost involved if I don't take it either. So I have a good deal of volume flexibility on the low side of the contracts. So I'm not sure exactly where you question is.

MR. HOWARD: Perhaps I can go a little further with that. You have three different types of contracts, the spots, the short-terms and the long-terms, correct?

MR. PHELPS: Correct.

MR. HOWARD: And, again, while you're dealing with volumes do I assume correctly that on a particular day in the future you forecast a need of supply of X MCF, or however you like to phrase it, that you want to find a price based on the terms of the contracts before you that you think is the best price going, correct? Or that will be the best terms going down the road when you need that supply?

MR. PHELPS: The firm contracts that we are discussing, the short-term and the long-term firm contracts are based on market indices. The price of the gas is based on market indices. It's not – we're not sitting today negotiating the price for January 5th. We're paying the market price that's determined at the beginning of January.

What we're really negotiating in these firm contracts is the premium on top of the index for the firmness of it, and in terms of getting the swing up and down capability of the volumes, and the right not to take gas if we don't want to. That's what we're really negotiating and the difference in the quality of the different contracts.

MR. HOWARD: If I understand correctly then, let us just look at the long-term contract that you contract to have available to you for so much gas. Do you at that point in time that you contract lock in on the amount purchase price for that gas, or will that price be based on the then market value?

MR. PHELPS: The price would be based on

then market value.

MR. HOWARD: At this point, and I will ask just for a little projection and perhaps speculation, if I may. For the duration of this winter given the current increases that we have experienced, what would be your projection as far as any additional increases, given the current condition of the market?

MR. PHELPS: I can’t make a prediction on that. You tell me what the temperature is the first 60 days of the winter and I’ll tell you – and I’ll guess at which direction it’s going.

MR. HOWARD: Fair enough. So that the public here can understand the increases that they have experienced and perhaps don’t realize that until they start getting their bills, if I can reference the customer choice program. I don’t know if that would be for Mr. Byars or not. Am I correct in that the program is being promoted in such a way that a member of the public can look at their per MCF charge and compare that with a marketer’s MCF charge in order to determine potential cost savings?

MR. PHELPS: That’s correct.

MR. HOWARD: At the time of the merger hearing, do you recall testimony indicating that the per-MCF charge of Columbia then was $5.14?

MR. PHELPS: I don’t remember, but it sounds reasonable.

MR. HOWARD: Would you accept that subject to check?

MR. PHELPS: Yes.

MR. HOWARD: What would that MCF charge be today?

MR. PHELPS: The gas cost – last quarterly gas cost adjustment filed and approved by the Public Service Commission was $6.83.

MR. HOWARD: Would you accept, subject to check, that that would be roughly 33 percent increase?

MR. PHELPS: Yes.

MR. HOWARD: And, again, based on projections that are nearly impossible to make, we don’t know whether there will be further increases over and above that during this particular winter season, correct? That all we know right now is that we’ve got a 33 percent increase and we don’t know if it will go any higher?

MR. PHELPS: Or lower, yes.

MR. HOWARD: Or lower. If I can present to you a hypothetical that we currently have a 33 percent increase that remains throughout the winter and that we have some folks who are financially pushed, if you will, in order to make payments on that. And the customer approaches you in that through the summer you have afforded that customer the opportunity to try to basically bring the balance down to zero.

But given those facts let's assume that that person is not able to do so and that we come into yet another heating season just a bad if not worse, would you be in a situation that you would reconnect that person so that they would have heat or would that depend on the circumstances?

That's the worse case scenario, but I'm trying to plan ahead. If we have volatile gas prices that continue and we have folks who through the summer were not able to bring their balance down to zero.

MR. PARR: Yes, we would make arrangements to reconnect that customer. As a matter of fact, currently there is a winter hardship reconnect program where we currently reconnect customers without requesting full payment of delinquent bills. So, yes, we would do that.

MR. HOWARD: Would there be additional charges, nonetheless, on that individual whether it's through late payment fees, et cetera, that could only compound their difficulty in making payment, or would that be on a given situation?

MR. PARR: No, there would be no late payment fees. We do not assess late payment fees on residential customers. So there would be no additional charges.

MR. HOWARD: That's all I have. Thank you.

MR. HOLMES: As I understand, we're talking about low-income customers at this point or their ability -- or are you saying any customer you would make that arrangement for?

MR. PARR: We wouldn't require full payment for customers. We would negotiate a mutually agreeable amount to re-establish service for that customer, yes.

MR. HUELSMANN: Okay, we'll try this once more. Mr. Seiple? Mr. Childers, did you have any questions?

MR. CHILDERS: I represent Kentucky Association of –

MR. HUELSMANN: Would you come up and have a seat. You've intervened in this case, right?

MR. CHILDERS: We've filed a motion to intervene. I've not received an order back yet granting that intervention. It was filed last week.

MR. HUELSMANN: Apparently it's on its way up and we'll let you ask questions. I apologize for that.

MR. CHILDERS: I just have one question, Your Honor.

MR. HUESLMANN: First introduce yourself and tell the court reporter where you're from and spell your last name, if you would.

MR. CHILDERS: Joe F. Childers, C-H-I-L-D-E-R-S, 201 West Short Street, Suite 310, Lexington. I represent Kentucky Association for Community Action.

In Columbia's response to questions posed by the staff both written and earlier in this hearing, Columbia said that it could support a universal service program for low-income customers under certain circumstances. Would your company be willing to support a program that called for a one dollar per meter line charge to create a fund for low-income energy assistance?

MR. PHELPS: We've been a proponent of a universal service fund for residential customers for several years now. And having said that, we have never really discussed a specific amount that would be a line or a meter charge. I think it's difficult to answer that question without seeing the entire bill, the entire legislation to see exactly how the universal service fund was put together. I apologize.

We just have never – we've never gotten to a per dollar figure.

MR. CHILDERS: Do you have any current proposals for a universal fund that you could share with the public or with any of the interveners? Have you worked up any sort of proposal that you could support?

MR. PHELPS: We have not. During the last general assembly session Senator Neil from Louisville introduced a bill, universal service fund. We agreed with many parts of that bill; conceptually, liked the bill, had some difficulties with some sections of the bill that I think need some working. And I think that we're more than willing to work with all interested parties to develop a universal service piece of legislation that might be introduced to the general assembly.

MR. CHILDERS: That's all I have. Thank you, Your Honor.

MR. HUELSMANN: Okay, we'll try this again. Mr. Seiple?

MR. SEIPLE: I have no further questions. Thank you.

MR. HUELSMANN: Ms. Mitchell?

MS. MITCHELL: No.

MR. HUELSMANN: Ms. Cheuvront?

MS. CHEUVRONT: No.

MR. HUELSMANN: That will conclude this part of the hearing. If you all would mind taking a seat over there. We're going to go to the next part, taking public comments. We would like the public comments, if we could, to be five to ten minutes at the most, if you can. The first one that we've got is the Cabinet for Families and Children and the Kentucky Association of Community Action apparently is going to have one person speak on both behalves. And if you would come up and sit down and state your name. Do you want to do it there?

MR. JENNINGS: Where would you like me?

MR. HUELSMANN: Why don't you go over here. It's a little bit better. State your name and spell your last name for the court reporter, if you would.

MR. JENNINGS: It's Clifford Jennings, J-E-N-N-I-N-G-S. I'm with the Cabinet for Families and Children Department for Community Based Services. Buy fuel or buy food? Buy fuel or buy medicine? Those are the choices that many of our low-income citizens, the elderly and disabled, may have to face and make this winter. These are not choices that we should be willing to accept.

The Cabinet for Families and Children administers the low-income home energy assistance program, that's LIHEAP, and contracts with the Kentucky Association for Community Action to operate this program, state-wide.

We are deeply concerned about the rising cost of fuel, especially the cost of natural gas for the low-income citizens of the Commonwealth. There are increasing indications that the price of home energy, that for natural gas, propane, fuel-oil, kerosene, wood and coal is going to go up this winter and has gone up.

With the gasoline prices remaining high the cost to deliver wood and coal are expected to increase by maybe ten percent. We expect to see that increase this winter. With natural gas prices predicted to increase by as much as 50 percent this winter from last winter, the lives of the elderly, the low-income, the disabled, families and children will be dramatically impacted. Low-income families, senior citizens, and the disabled will be forced to make that choice. That is to buy fuel, buy food; or buy fuel or buy medicine.

If this winter is extremely severe or there are extended periods of very cold weather, this problem will be even more critical and could reach a dangerous level. Studies show that the low-income households spend between 14 and 18 percent of their income on average for heating costs in the winter.

For example, a family of four with a gross income of – that's gross income – of $1,200 a month, which is roughly 85 percent of poverty, would spend from $170 to $250 a month in the winter for their heating cost.

If we have the kind of increases that we're talking about here, that could be a very serious impact on those families who are already paying a significant portion of their budgets for then energy costs.

Conversely, the other households, the average household in Kentucky pays from three and a half to seven percent of the household income for heating costs. Studies show that the elderly are likely to pay their heating bills at the expense of their food and medicine.

Nationally, LIHEAP is insufficient to meet the demands, especially in the face of these increased energy costs this year. Under LIHEAP, only those who have income below 110 percent of poverty are eligible for help. There are many more working families out there who are likewise going to feel the impact of these cost increases.

Those who are above 110 percent of poverty do not qualify for LIHEAP. For those who are eligible the LIHEAP benefit is small compared to the actual cost of heating their incomes (sic). In subsidy last year the average one time benefit, taking into account all the fuel types, was $92. And last year we served over 94,000 households in that component. For natural gas the average benefit was even lower; it was $82 one time.

In the case of a family of four, let’s assume that they heat with natural gas, their heating costs for the winter months would cost from $840 to $1,080. With our crisis component the maximum benefit for natural gas was $100.

To what extent will these benefits assist a family if natural gas prices increase by 50 percent? Last year in our crisis component we had 48,376 households served. Individuals, especially the elderly, are becoming worried, even frightened about the prospect of higher heating bills this winter. They have heard the news reports. One senior citizen states, I am on a fixed income and cannot save for a big increase in my gas bill. My medications cost almost $300 a month. What am I going to do?

Kentucky is faced with significant funding issues. Only those with annual incomes at or below 110 percent of poverty receive help with LIHEAP. The LIHEAP benefits will only cover a small portion of the winter heating costs.

Now many have heard that President Clinton has released emergency funds and we are extremely grateful for that release of the funds so early in the year. I just want to clarify, however, that these funds are not new dollars but are advanced releases of emergency funds that are appropriated annually for the president to release in times of weather related emergencies.

Other than Winter Care there are no other significant sources of funds available. And our most vulnerable populations who are dealing with fixed or limited resources are struggling with these increased energy costs.

We cannot do it alone. We need community involvement in addressing this issue so that no one has to choose between buying fuel or buying food; buying fuel or buying medicine.

How is the state addressing this problem? One thing we're doing is we're attending hearings such as this and speaking out. We're also facilitating two other sessions, which will address not only the natural gas issue, but the increased cost in all the other fuel types.

We're asking community resources to become more involved and lend a helping hand with this situation. Governor Patton joined with other governors and asked the President to release the LIHEAP emergency funds before the winter begins instead of later when we're in the midst in the energy - the high heating cost period. And as a result of that on September 23rd, the President released 400 million of these emergency funds to all the states. Kentucky's share of the emergency's fund is 4.7 million. But that is not enough.

Supporting increased federal funding for LIHEAP and weatherization program is another thing that we're still working on and still want to see in appropriations for the block grant itself. The other thing that we want to do is to encourage the utilities to maintain humane cutoff policies. And we encourage citizens to make contributions on their monthly utility bill to Winter Care, which will assist the low-income households.

State and Community Acton Agencies cannot do it all. There must be a coordinated state-wide effort. Therefore, we are asking all community resources to help, from elected officials to church groups to private sector to utilities to civic organizations to private citizens to anyone or any group in a community who can help keep a citizen from freezing this winter. That is providing resources. And these could include blankets, emergency shelter, space heaters, or assisting in helping a person paying their energy bill.

These community resources already help. But I would like for them to dig deeper and help more. Thank you.

MR. HUELSMANN: Thank you, Mr. Jennings. I think the next person is Mr. John Davies from the Cabinet for Natural Resources and Environmental Protection. He's the director of the Division of Energy.

MR. DAVIES: Good evening, I'm John Davies, D-A-V-I-E-S and I'm from the Kentucky Division of Energy which is part of the Kentucky Cabinet for Natural Resources and Environmental Protection.

And first I'd like to thank the Public Service Commission for allowing us to comment this evening. It's been a very full evening and because of that I'll make my remarks brief and hopefully helpful.

Our purpose this evening is twofold. First I would like to explain who we are in our role of energy within the commonwealth; and second, which is perhaps more important, to highlight what families and businesses can do to reduce their energy bill through simply an effective energy conservation practices.

The Division of Energy is a state agency whose mission is to promote healthier and more prosperous and sustainable future through the wise use of energy. The division's history extends more than 25 years, originating in the early energy crisis of the 1970's when National Energy Security and energy conservation issues gained public attention. Since its inception the Division of Energy through the partnership with the United States Department of Energy has helped Kentucky Schools and hospitals save an average of 25 percent on energy costs in over 1,100 buildings. We've developed an energy efficiency program for state government buildings, promoted the use of alternative fuel such as compressed natural gas and ethanol, and we prepared for and responded to emergencies, energy emergencies to lessen their impact.

These are just a few examples of our

programs. And while our mission remains the same our focus changes from time to time to respond to energy issues and challenges.

Today, despite great gains in energy efficiency we have made over the years, our state and nation still confront serious energy issues that affect our economy, health, and environment. The approaching winter season presents us with such a situation.

As a non-regulatory state agency, the division works with others on a voluntary cooperative basis to ensure that energy emergency issues are resolved. We promote contingency planning on both the part of individuals and organizations to anticipate and reduce the impact of energy problems. Most everybody recalls the efforts to prepare for the new millennium. The Division of Energy was one of the key agencies working on and inner agency task force to plan for energy problems that could have arised - arose or resulted from Y2K.

We have also partnered with the Division of Emergency Management, energy suppliers, other states, and the federal government to resolve energy supply and distribution problems caused by severe winter conditions. We did this as recently as of January

2000. I see our current situation as requiring a similar effort to prepare for problems that may arise from higher energy prices and tighter supplies.

The Division in conjunction with five other state agencies has formed a winter fuels working group to determine how the state government can best prepare for potential energy challenges ahead. The other agencies are the Public Service Commission, the Kentucky Division of Emergency Management, the Office of the Attorney General, the Cabinet for Families and Children, and the Cabinet for Economic Development. And that's all under the purview of the governor's office.

Our winter fuels working group will address such issues as attainable, reliable information under energy supply, demand, and prices through the Commonwealth, reviewing and updating Kentucky's existing emergency operation plans as they relate to energy supply, coordinating appropriate response among state agencies and working with other states and federal government and non-governmental organizations to implement solutions.

This hearing focuses specifically on natural gas. But all of us who have bought gasoline, read the newspaper, or heard a news broadcast in this past several weeks are well aware that the cost of oil is near record highs. Prices for petroleum products whether they're gasoline, heating oil, diesel fuel or propane are determined on the world market. And this market has risen steeply.

In less than two years a barrel of oil sold for about $10. In recent weeks that same barrel of oil brought nearly four times that much. Tight supply and higher natural gas costs may lead to even higher prices for our other heating sources such as heating oil and propane. Together these three products, heating oil, natural gas, and propane, heat 59 percent of Kentucky homes.

While the heating cost may be up 20 to 40 percent this winter, we can save an equal amount by adopting energy saving practices. And let me share some of these common sense tips with you. And I must admit that these are not glamorous, but nonetheless they do work and they have a proven track record.

Just as a side note, we've provided some publications, and they're available outside on the table that include these as well as some other energy saving advice.

First, keep your furnace tuned and in top condition. Proper maintenance of your furnace can save six to ten percent on your heating bill.

Second, weatherization. Weatherize your home to prevent heat loss. Apply caulk and weather stripping around all of your windows, outside doors, or where plumbing and electrical wiring penetrate doors, walls, floor, and ceilings. By sealing leaks you can save 10 to 25 percent on your heating bill.

Next, control temperature in your home. Keep the thermostat on the lowest setting which is comfortable. Each degree you lower your thermostat you can save two to three percent on your energy bill. If you set your thermostat back from 72 degrees to 64 degrees for an eight hour period, and those are the hours you're away from the home during the day, you can save five to ten percent on your heating bill. Use a programmable thermostat so you don't need to adjust the thermostat by yourself. The energy savings will pay for the cost of the programmable thermostat over the long run.

Add insulation in your attic. Most Kentucky homes should have at least an R30 insulation level in the attic. If you increase your R19 insulation to an R30 you can save another 15 percent on your heating cost.

Water heating typically accounts for 14

percent of your utility bill. Repair leaky faucets insulate the water heater tank hot water pipes and you can - the water heater thermostat, you turn that down to 120 degrees and install low flow faucets and showerheads can save also on your water heating cost.

On sunny days let the sun do the work. Open curtains and shades to allow sunlight into your home and close them at night.

When the fireplace is not in use keep the flue damper closed tightly. Fireplaces are not efficient energy sources. Although they warm the surrounding area, they also draw much of the heat out of your house up the chimney. A reminder if you use your fireplace is have it inspected annually.

Adopting these measures can help you lower your cost of heating your home while increasing your comfort during the winter. Other measures you can take to reduce your energy costs include buying high efficiency energy star labeled products when replacing appliances and equipment.

Many of these energy saving tips such as adjusting thermostats, reducing hot water temperatures, sealing duct work, performing routine maintenance on furnace equipment apply to businesses and industry as well. Ask employees to help out by turning off lights in unoccupied areas, keeping exterior doors closed as much as possible, and turning off equipment and machines when not needed. These all can generate significant energy savings.

If you are a commercial or an industrial natural gas customer on an interruptible contract, make sure that your standby equipment is working properly and you have adequate supplies of standby fuel on hand or under contract for delivery.

Remember in the unlikely event that we do experience actual shortage of natural gas, other interruptible customers are going to need the same fuels that you will. Also be sure to stay in close contact with your standby fuel supplier.

As I said, energy conservation is not glamorous but it does work. Those in our communities who can at least afford higher energy prices might be faced with difficult decisions. We recognize the choices many low-income households will face. Pay for energy or pay for food or medication or life’s other necessities.

There are not easy answers, especially in the short run. And all of us together need to start working on those actions that will make us less dependant on foreign oil and more energy self sufficient. Energy efficiency and conservation are steps in that direction.

As I mentioned earlier, in the back room we have some publications with more tips on saving energy in homes and businesses. Our toll free number and web site are also provided.

The Internet is a tremendous resource for finding energy saving conservation ideas and energy efficient equipment. And I encourage you all to visit our web site to link to these and other sites.

I would like to recognize Columbia Gas for its initiative to include energy conservation tips on their web site.

This concludes my comments for this evening and I thank you for your time.

MR. HUELSMANN: Thank you, Mr. Davies. One of the nice things about being chair is you can deviate from the schedule. My understanding is Kip Bowmar would like to say a few words at this point on behalf of the Kentucky Association of Community Actions.

MR. BOWMAR: Thank you, Mr. Chairman. My name is Kip Bowmar and I'm the executive director of the Kentucky Association for Community Action. We operate the low-income home energy assistance program with a grant from the Cabinet for Families and Children and subcontracted to the 23 community action agencies around the state. And in addition to Mr. Jennings' comments I wanted to just amplify a few comments about the extent of the need that exists in the state.

Last year with LIHEAP we got some emergency summer cooling dollars. And even with all of those dollars we served about 184,000 households last year, which was the largest number we had served in several years. And that still only represented 60 percent of the eligible households at or below 110 percent of poverty. So we know that there's a great deal of need out there.

And the other thing - the other part of the story that does not get told with that are the number of families and households that are between 110 percent and 200 percent of poverty or what we define as the working poor that aren't eligible for LIHEAP or a number of other programs.

So we do believe that a universal service program is necessary to help address the energy needs, not just this winter in Kentucky but in on-going winters because you can - with any time you've got a commodity where prices can fluctuate wildly in the laws of supply and demand we need to have other resources available.

That being said I think I would also like to salute Columbia Gas for being a good corporate customer with their customer assistance program and a number of the things that they do in the community to try and help their low-income customers and encourage all utilities to take steps in that direction. But we do need, I think, a universal service program that can help address the needs, not only of the households that are up to 110 percent of poverty, but households that are beyond that that may not be able to get assistance.

Also I would like to put out KACA's 800 number so a client or a person has a question about where they can get energy assistance or weatherization in their county, they can call the Kentucky Association for Community Action at 800-456-3452 and we can make a referral to any local service provider in any county of the state for customers or clients who may be interested.

Basically, that concludes my remarks. I just wanted to add a few words and I thank you for the opportunity to speak.

MR. HUELSMANN: Thank you, Mr. Bowmar.

That’s spelled B-O-W-M-A-R, for the record. Next group is the Community Action Council of Lexington-Fayette, Bourbon, Harrison and Nicholas Counties. This is Jack Birch.

MR. BIRCH: Thank you, Mr. Chairman, members of the commission. My name is Jack Birch, I am the executive direction of Community Action Council. It’s a four-county agency located here in Lexington. And I’m also here in my capacity as president of Winter Care Energy Fund.

Community Action Council through both public and private resources provides approximately 95 to 98 percent of all low-income energy assistance in Fayette County. There are some other sources, this is primarily some churches and some other operations. But we have – because of the size of our operation in the low-income energy area we have a pretty good perspective on the issue and the resources.

I’d sort of like to start out by also thanking the company. Columbia Gas of Kentucky is providing currently approximately $200,000 a year in shareholder funds for its low-income customers. I think it’s a phenomenal number if you take a look at their total size of the company as you compare them really to any of the investor-owned utilities in the area.

I want to try to put a little bit of a human face on some of the numbers we've been talking about tonight and some of the elements we've been talking about tonight. Within Fayette County - and I'm going to stick with Fayette County alone because our service territory is a bit bizarre - there are 9,000 Columbia Gas households with incomes below the federal poverty level. That's 9,000 households. Those household's average low-income annual cost for service of Columbia Gas is approximately $860.

If you take the recent price increase you're adding to the $860 another $170 per household. Or basically you're taking 1.6 million dollars from households that are at or below the federal poverty level. Now, the federal poverty level is the minimum amount a household can survive on. Most households at or below the federal poverty level are not at the federal poverty level. Some of them are as low as 15, 20 and 25 percent of the federal poverty level. So we're talking about $170 per household, 1.6 million dollars in this county alone for families that already have incomes that the federal government say are below the minimum necessary to survive.

It seems as though everybody is a little bit reluctant to predict what's going to happen to pricing in the coming winter. But our reading of the - - and I will admit this is the popular press, the *New York Times* and sources like that, the *Washington Post*, indicates the potential, the possibility depending on supply and on demand and on the severity of the winter – that potentially we could see another 20 to 50 percent increase before we get through the heating season that's ahead of us.

If we see another 20 percent increase again those 9,000 households – the total hit is going to be $240 on an annual basis or 2.2 million dollars for households in Fayette County who live below the federal poverty level.

We see a 30 percent increase, we're talking $275 per year for those households or two and a half million dollars. And if we get a 50 percent increase – and admittedly, I've only read one source that says we'll see that again this heating season – we're talking $345 a year or 3.1 million dollars.

We really are talking about choices between paying for you utilities or paying your rent or feeding your children or buying your medications if you're a senior citizen.

The price increase we've already undergone is going to be an extreme burden on the poor. If the weather gets colder and last – we've been very lucky the last two winters. If we have a really cold winter it's going to get worse. The dollar figures I've given you will go up.

We do have – I think there is some light out there. Community Action Councils are presently trying to aggregate into a buyer's club of low-income customers to negotiate with the marketers in the choice program. And depending on the extent to which we can bargain and reduce prices we may be able to mitigate some in the other direction. That's certainly our intent. We've set a goal ourselves of trying to produce five to ten percent better than what individual households dealing with marketers are able to obtain.

I'd like to sort of now get you to take a look at the numbers I shared with you in terms of the impact of this increase when you look at low-income energy assistance in this county. And if you keep in mind that the current increase is going to hit these households at about $170 per household per year, if we see an increase of as much as another 50 percent we're talking $345.

The LIHEAP subsidy, and that is a payment to a household based solely on income. They can come in if they apply; they meet the income criteria then a payment will be made to Columbia Gas. The LIHEAP subsidy in Fayette County last year averaged $70. The $170 increase we've already seen is significantly higher than the average payment that they received last year.

The LIHEAP crisis program, the maximum benefit that was allowed of a household was in crisis was $100. We averaged $100 during the crisis program.

The Winter Care Program averaged approximately $100 per households who came in for assistance. And those were households who had already exhausted their entitlement to public benefits.

The customer assistance program, which Columbia Gas and Community Action Council operate together, and which served approximately 483 households on average, assisted each of those households with about $420 on an annual basis.

Just to make those programs whole, assuming nothing else, just to be exactly where we were a year ago at the current increase it would take $65,000 not likely to show up in this county. And if you started looking at that on a state-wide basis you're talking very large numbers. If we do see something as much as a 50 percent increase, just to keep those programs and those households whole we're talking $130,000.

Now, I want to point out those households that received assistance that was only approximately 1,900 households out of the 9,000 who were eligible. The other 7,000 did not come in for help. With these kinds of increases that we have seen and the kinds of increases that we could see we have to assume a certain number of households will now get kicked into the category of, can't handle it any more, got to go look for some assistance.

We're conservatively estimating in collaboration with the city, the Division for Community Development and Housing, that the need in Fayette County alone this coming winter will be at least $275,000 just to keep households in the program approximately where we are today.

I don't have any real solutions. I was asked to try to figure out some solutions. I think one is just public awareness. And I do appreciate the Commission holding these hearings. It will make people - it will make elected officials aware of the problem. Public resources, I don't personally hold out much hope for Congress. I do think that it's a possibility that our local government here in Fayette

County, we're a fairly affluent county, will come up with some resources to make up part of this.

As the administrator of Winter Care state wide, we certainly hope that people will consider that as they pay their bills. It doesn't take very much for – I believe the company has 140,000 customers, a dollar a customer that's $140,000 a month in contributions. So very little contribution from households can make a big difference.

And, of course, we strongly support the concept of a universal service fund. If you're in the kind of work that we do, you're constantly sitting around and waiting for Congress to decide how much money they might provide. And they still haven't completed their deliberations on the fiscal year that started October 1. And you're crossing your fingers and praying that people will provide assistance through programs like Winter Care. A universal service fund would make a tremendous difference because it would rationalize programs. It would allow us to think through and plan ahead.

I thank you very much, Mr. Chairman.

MR. HUELSMANN: Thank you, Mr. Birch. The next person is Daugherty Resources. It's my understanding it's Mr. Bill Barr. If you give us ten second to walk out so we can watch your presentation.

MR. BARR: That would be great. Would you mind – do you care if I use this table so that I may sit?

MR. HUELSMANN: That’s fine.

MR. BARR: For the record, my name is William Barr and vice president of Daugherty Resources. That’s B-A-R-R. Daugherty Resources is appreciative of the Public Service Commission’s hearing that they’re having this evening. I would like to thank the chairman, the vice chairman and Commissioner Gillis as well as representatives of Columbia Gas and member of the various public advocacy groups.

In making this presentation I would also like to acknowledge the assistance of the Kentucky Division of Oil and Gas, the Kentucky Oil and Gas Association, the Interstate Oil and Gas Compact Commission, and the National Petroleum Council.

Our goal tonight is to present an industry perspective on the current market situation that exists in the United States. I’ll start my presentation by reading a quote from Bill Richardson, the Secretary of the Department of Energy, in a letter addressed to the National Petroleum Council. “For a secure energy future, government and private sector decision makers need to be confident that the industry has the capacity to meet the significant increases in natural gas demand for the forecasted twenty-first century.” I was afraid that was going to happen. Will this mike move over here?

It’s our position that there is no energy crisis. The long-term supply of natural gas is not in question. In fact, what we’re currently experiencing is price shock from the workings of supply and demand.

One point that should be noted is that while crude oil and the supply of crude oil is a global issue, natural gas is not. It’s a continental issue. Eighty-seven percent of our natural gas, which is consumed in the United States, is produced here in the United States with the remaining portion coming from Canada and Mexico. As I said, this is price shock. The price of natural gas is higher today because of existing market conditions. Fortunately the law of supply and demand is working. And price is the symptom, not the problem.

This slide, which is courtesy of the National Petroleum Council, was contained in a report dated December of ’99. I call your attention to the National Petroleum Council’s projected (sic) for prices for the year 2000, three dollars. Not the five dollars that we're currently hearing. And these are prices at the wellhead or actually into the wholesale market.

Something that I did not hear tonight in any of the other presentations is what the real price of natural gas is when adjusted for inflation. Let's project that natural gas is going to be $8.80 this winter delivered with – and this is to the retail residential market. Using that assumption and adjusting for inflation going backwards from 1999 dollars, I invite you to look at the price that America paid for natural gas in 1986.

At the same time I would suggest if you look at the price that you paid for a home in 1986 you've enjoyed a 200 to 300 percent increase in the value of that home. While your natural gas bill is even with the dramatic increase we're expecting this winter constant with 1986 prices. By sector, using that same adjustment for 1999 dollars, that means the residential cost of natural gas is 30 percent less than it was in 1985.

We believe there are four specific conditions at work in the marketplace. The first is the effect of low levels of drilling activities during the recent past and specifically the last three years.

This chart depicts drilling activity in the lower 48 states from 1991 current through 1999 and forecasted by the National Petroleum Council through 2015. You'll see in 1997 a precipitous drop through -- running through the summer of 1999 when wells dropped from 30,000 to approximately 23,000.

During the same period of time, from 1990 to the year 2000, this chart depicts the annual decline in existing reserves. And that's the aqua color in each of the bars. The center yellow depicts additions to reserves during that period of time. And the right-hand color – this may be green, I'm a bit color blind – and the right-hand color which is yellow shows a rig count during that same period of time.

You'll see the rig count has been from 1990 through 1999 – that's almost constant with fluctuations down and upward. Although projected now, this chart is somewhat aged. The 650 is not the current number running, but rather the number needed to keep production flat during the year 2000 given the increase in demand.

Specifically I want you to look at 1999. This is in billion cubic feet a day. This country added 2.2 – was short in adding 2.2 billion cubic feet a day to its new reserves while it was producing and its existing reserves were declining at that rate of 13.2 billion. So we were using existing reserves at a far greater rate than we were adding them.

The second condition, which we believe is important, is the increase in demand for natural gas. Again, this is a National Petroleum Council's slide which projects – shows a projection going from about 18 TCF in the year 1990 to in the year 2000 projecting to be in the 22 and a half range. Most estimates have by the year 2010 demand approaching 30 TCF in this country, or an increase of 50 percent.

The same slide just a little different. This is consumption – factual consumption from 1986 moving forward through 1999 and estimated for 2000. It's a basic growth of three to four percent per year. By sector residential has not changed dramatically. Commercial – nor has commercial. The big change has come in industrial and in electric generation. Specifically, electric generation is projected for the period from 1998 to 2010 to increase by 47 percent while commercial and residential together only increase by 30 percent with industrial being the remaining 23 percent. Electric generation increasing by 47 percent in terms of its demand on natural gas.

The assumptions behind that are that the GDP will grow at two and a half percent per year, that 140 gigawatts of new power will come on-line by 2015, 70 percent – off this chart, 97 percent of all planned and under construction electric generation is planned as we speak to be powered by natural gas.

The National Petroleum Council projects that 70 percent of those new projects could switch fuel. They also project no nuclear facilities and the 30 gigawatts will be up for re-licensing of nuclear facilities; only half of which will be extended and the other half or 15 gigawatts will be retired.

The third condition, reduce short-term deliverability. From 1994 to 1997 this country's natural gas production has basically been flat while its consumption has risen at three to four percent compounded per year.

The outlook for North America, again, with a – we have an evening off or a stability in production, projection of production even declining in the year 2000. Canadian production, keep in mind they make up approximately 13 percent of our natural gas that we consume in the United States, growing slower than expected. We must shift the demand – our focus to demand.

The final – and I won't spend much time with this, it's a very complicated issue – but because of the increase in price there's an issue with storage of natural gas. For those of you in the public that don't know, natural gas unlike crude oil, unlike fuel oil or propane cannot be stored above ground. It's stored in depleted reservoirs around the country connected to the interstate pipeline transmission system.

Historically we have stored 20 percent of our annual demand in natural gas below ground in these storage facilities. Two factors are at work that are changing the level of storage. One is the amount of natural gas being used to generate electricity. Keep in mind that electricity's peak demand period is at a period when natural gas was typically at its low period, the summer cooling months.

As electric generation increases, its use of natural gas as its fuel of choice, less and less natural gas will be available to go into storage in the summer months, and in particular at the historical low prices it once was available.

Who produces the natural gas in this country? In the press often we hear and read about the big natural gas – or the big energy companies. In fact, 73 percent of all the natural gas in the United States in produced by independents, not by the majors. In fact, in Kentucky there is little production by the majors.

What is an independent producer? It's a producer of natural gas that operates solely in the field of exploration and production. They typically do not process natural gas into other products or sell their production on a retail basis. They range from companies as large as Devon and Anadarko to small – which are large public companies – to small privately held companies such as the 200 companies that make up the Kentucky Oil & Gas Association.

The Commissioner asked a question earlier regarding the number wells and the production in the State of Kentucky. The yellow line and the numbers on the right represent the volume of natural gas produced in Kentucky. Currently we're producing about 78,000 BCF a year. Interestingly enough, and I don't have it on this chart, in the same period of time we're consuming in Kentucky over 90 BCF - - 90,000 BCF. The number of wells drilled is represented by the red columns. You see the reduction in the number of wells drilled in the State of Kentucky with the decline in prices reaching a low in 1997. Interestingly enough our low for gas prices was December of 1998 or in that – I'm sorry, in 1998 that price was below two dollars.

Natural gas consumption and production. I point out that the information for this chart came from the Energy Information Agency of the Department of Energy on the U.S. level. And I cannot explain the precipitous increase from '99 to '98. We've been relatively flat in the 95,000 BCF since '98 and '99. They project or they report through August of this year that we had already in Kentucky consumed 98,000 of BCF of natural gas. During the same period of time we produced and we're estimating we will produce approximately 90,000 BCF.

There are several components to a healthy oil and gas industry, the availability of skilled workers which is becoming a problem because of years and years of decline in the work force; adequate financial returns which we are now seeing during this upturn in prices; availability of drilling rigs; access to public lands which is a U.S. and national issue of some significance. It's being debated in the presidential election as to where to give it increased access to the East Coast, the Gulf Coast, the offshore California, and the North Alaskan areas.

An area that is of significance is that

there be no unnecessary government restraints. During periods of high price when you hear the stories of the poverty – those members of our society, in particular our home town, that are unable to pay their gas bills, there is a movement that always comes forward to bring about governmental restraint on prices.

We suggest to you that to do so results in what we called – and actually I can’t take credit for this – Ken Lay (phonetic) the CEO of ELG which is the spin off of In-Ron (phonetic) Oil and Gas presented this at the governor’s summit last week in Columbus called by Governor Knowles of Alaska and Governor Taft of Ohio.

During periods of tight supply when the price surges there’s a tendency to want to put price caps on natural gas, or any commodity for that matter, which then tightens supply, creates more demand, results in regulated shortages and then curtailment.

That ends my formal presentation. In concluding I would suggest to the Public Service Commission they are doing the right thing in making the public aware of the increase in the price of natural gas. I suggest to you, however, you should not consider price constraints or controls of price and let the marketplace work. The rigs are running at an increased pace as a result of that. More supply will come on the market and the prices will drop. Thank you.

MR. HUELSMANN: Thank you. Would you have a copy of that?

MR. BARR: I have a copy. I will deliver a copy in a gray tone, but I will submit a color copy, which is better at a later date.

MR. HUELSMANN: If you would put that in the record. I don't know if we can get in on the Internet but we'll worry about that later. Let's take just about a three-minute break. We need to change the tape once again.

(OFF THE RECORD)

MR. HUELSMANN: The Propane Gas Association couldn't be with us today, but our understanding is the price of propane will increase with the price of gas.

Next we have our new division director Jenny Smith, the Division of Consumer Services for the Public Service Commission. Jenny.

MS. SMITH: Does it matter which mike? Good evening, I'm Jenny Smith and I'm the Director of Consumer Services. I'm going to take a few minutes to tell you about – give you a little bit of history on the commission and the consumer service's staff and how to reach us if you have a complaint.

First, I would like to give you a history of the PSC. The PSC was created by the General Assembly in 1934. It consists of three commissioners, all of which are present here tonight, and they are supported by a staff of over 100. The staff includes engineers, financial analysts – I forgot – but anyway, we do have a Consumer Service's staff and that's where we can help the public.

We take complaints daily. You can reach us by calling the 800 number, the regular line, by fax, e-mail, or you can visit us at 211 Sower Boulevard. We are always available by e-mail 24 hours a day. If you get home after 5:00, we'll read it the next morning at 8:00.

What we do is when you contact our investigators the first thing we ask is have you contacted your utility. The utilities like to have an opportunity to resolve their complaint before we get involved. After you say yes or no, we either refer you back to the utility or at that point we will begin to proceed with our investigation.

That will require some information from you. It requires name, address, telephone number. Some people say, well, why do I have to give you my phone number, it's unlisted. Well, how are we going to call you back. So at that point they do agree to give us the phone number.

Then we ask them – we try to identify their problem because when they first call not all of them are aware of the problem. They think they know what their problem is, but they have no idea why they are in this situation.

We contact the utility, we try to resolve the complaint; but we only have certain tools to work with. And those tools are the Public Service Commission regulations and rules, the Utility Tariff and the Kentucky State Statutes. So we are not going to satisfy all of the consumers because we have to work within those guidelines.

Hopefully when we are – when we've concluded our investigation the process has been resolved. And if they're not satisfied they better understand the commission's role, the utilities role, and their place in the process. So, you know, hopefully they're going to be back again. We have regular repeats, believe me.

Then what I would like to talk to you about is how you can reach us. And I think there's a brochure out on the table out back. And you can reach us by the 800 number, 1-800-772-4636 or our regular number, 502-564-3940. You can reach us by fax, 502-564-7397. That comes straight to the Consumer Complaints. You can reach us by visiting us as I just said at 211 Sower Boulevard, by letter, or by the hotlines.

Thank you for giving me this few minutes to talk to you about the agency. And I'm going to turn the program back over to the Chairman.

MR. HUELSMANN: Thank you, Jenny. One of the things I learned from coming to PSC is an easy way to remember our 800 number is 1-800-PSC-INFO and it works very well. Thank you.

Comes time now for statements and comments made by the public. I noticed a considerable amount of the public has now departed at the last little break we took. But I believe there's a David Walker who is signed in and said he would like to say something, or may like to say something. Is Mr. Walker here? No. Any other person with the public that would like to make comments at this point?

Okay, hearing none it comes time for closing statements, if any. And I guess the easiest way to do this is in reverse with Ms. Cheuvront first.

MS. CHEUVRONT: Yes, I have a brief

statement.

MR. HUELSMANN: Go ahead.

MS. CHEUVRONT: We really appreciate the forum by which you all have chosen to have this. It's nice to hear public comments and to see if there's some impact that we can make on these natural gas increases.

This is affecting everybody, not just in Kentucky, but all over the United States, the low-income, as Kip referred to the working poor, the low middle class. These people that don't – they don't have the opportunity for assistance. All we hope is that in hearing all these comments that the commission will consider all the alternatives before doing anything that may increase a bill that is already increasing. Thank you.

MR. HUELSMANN: Thank you. Ms. Mitchell?

MS. MITCHELL: No.

MR. HUELSMANN: Mr. Seiple?

MR. HUELSMANN: No. I would just refer the commission to the opening statements of Mr. Phelps and Mr. Byars for our positions.

MR. HUELSMANN: Thank you. Last but not least, is my comments and I'll make them short. Mr. Kelly, I thank you for having being here and your staff being here and the excellent presentation that they made. The Commission on behalf of the other two commissioners as well as the staff believe this is a very serious issue that we're facing and we need to address the issue, if possible. We need to do whatever we can in this regard. So we think it's an extremely serious area.

We're going to hold hearings in all five parts of the state by our five major utilities so that they can express themselves and the people that they serve can be in attendance.

Last I'd like to use the statement, working together we can make Kentucky a better place to live and that's why we're here. Thank you all for your attendance. Appreciate each and every one of you being here. That concludes the hearing.

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